<u>Date – 27 August 2022</u>

Acceleration in Bank credit growth

GS Paper 3: Indian Economy and issues relating to Planning, Mobilization of Resources, Growth, Development and Employment; Inclusive Growth and issues arising from it.

News: RBI data showed that Bank credit growth accelerated to 14.2% in the quarter ended June 2022 from 6% in the same period of the previous year outpacing deposit growth.

What is the meaning of Credit Growth?

- **Rise in demand for loans is called credit growth.**
- Credit growth is measured as the **annual percent change in total outstanding loans of individual banks**, while the soundness of banks is measured by their distance to default.

What is the meaning of deposit Growth?

- Deposit Growth means the rate of annual growth in an entity's deposits, other than certificates of deposit (or other similar deposit instruments), for a fiscal year.

Importance of Credit Growth for banks:

- **Credit Growth is an important indicator of economic activity.**In exchange for the money you deposit in your bank account, banks promise to pay you a regular interest. The longer the tenure of your account, the higher is your interest rate. This is because your deposits are a source of cheap funding for banks. It has to pay you only 4-6% on your savings account deposits. This is lower than the 8% it pays when borrowing from the RBI. Banks then lend the money for a higher interest rate. This earns banks an interest income. The higher interest payments help banks make profit.

What is the credit-deposit ratio for banks?

- The **CD ratio** refers to the credit-deposit ratio in banking parlance. It tells us how much money banks have raised in the form of deposits has been deployed as loans.
- So, if the CD ratio for a single bank or whole banking system stands at 75%, it means that three-fourth of the deposits with that bank or with the system has been given out as loans.

Why is the CD ratio important?

CD ratio denotes the value of loans given as a share of deposits held by banks.

- A low CD ratio suggests relatively poor credit growth compared with deposit growth.
- A high CD ratio would mean strong demand for credit in an environment or relatively slower deposit growth.CD ratio had slipped to historic lows of under 70% during demonetisation.

What are the reasons for credit growth?

- **Financial deepening:** When Credit grows faster than GDP as an economy develops then financial deepening happens.
- **Normal Cyclical upturns:** Credit growth can happen or grow faster than GDP when firms' investment and working capital needs fluctuate with the business cycl**e.**
- **Excessive cyclical Movements:** When stock prices shoot up, as in case of credit boom firms' net worth rises sharply. Banks may then be tempted to lend more.

Key findings from 'Quarterly Statistics on Deposits and Credit of SCBs for June 2022'by RBI

- **RBI data showed that Bank credit growth accelerated to 14.2% in the quarter ended June 2022 from 6% in the same period of the previous year, outpacing deposit growth.**
- **India has witnessed broad- based Credit growth:** All the population groups (i.e., rural, semi-urban, urban and metropolitan), all the bank groups (i.e., public/private sector banks, foreign banks, RRBs and SFBs) and all the regions of the country (i.e., central, eastern, north-eastern, northern, southern and western) recorded double-digit annual credit growth in June 2022.
- **Aggregate deposit growth (year-on-year)** has remained in the range 9.5 – 10.2% during the last five quarters.
- **Metropolitan branches** continue to **account for over half of the bank deposits** and their share increased marginally over the last one year.
- The **share of current account and savings account (CASA) deposits in total deposits** has been **increasing** over the last three years (42% in June 2020, 43.8% in June 2021 and 44.5% in June 2022).

- As **credit growth is outpacing deposit growth** in the recent period, **credit-deposit (C-D) ratio has been on the rise**, the data showed.
- In June 2022, **C-D ratio stood at 73.5% at all-India level (70.5% a year earlier**) and 86.2% for metropolitan branches of banks (84.3% a year earlier)

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